

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF CHARTER NETWORK)	
COMPANY TO EXECUTE A PROMISSORY)	
NOTE TO LITEL COMMUNICATIONS, INC.)	CASE NO. 90-094
IN AN AMOUNT NOT TO EXCEED)	
\$18,750,000)	

O R D E R

On April 11, 1990, Charter Network Company ("Charter") filed an application requesting Commission approval of its execution of a promissory note to LiTel Communications, Inc. ("LCI") in an amount not to exceed \$18,750,000. Charter is a wholly owned subsidiary of LCI.

Charter (formerly known as Phoenix Network Corporation) was authorized to provide intrastate interLATA long-distance telecommunications services within the Commonwealth of Kentucky in Case No. 89-288.¹ In Case No. 90-016,² Charter and LiTel Communications Corporation ("LiTel") were authorized to enter into certain credit arrangements including cross-guarantees. LiTel was

¹ Case No. 89-288, Application Of Phoenix Network Corporation For A Certificate of Public Convenience And Necessity To Provide Long Distance Telecommunications Services Statewide As A Reseller Within The Commonwealth Of Kentucky.

² Case No. 90-016, The Joint Application Of LiTel Telecommunications Corporation And Charter Network Company For Authority To Enter Into The \$25 Million Revolving Credit Facility, To Execute Cross-Guarantees, And For Authority To Execute Related Documentation.

authorized to provide intrastate interLATA telecommunications services in the Commonwealth of Kentucky in Case No. 10090.³ LiTel is also a wholly-owned subsidiary of LCI.

The note will be payable on or before January 5, 2000. According to the application, payments on the note by Charter to LCI will secure for Charter the benefits of the LiTel System. Some of the benefits available to Charter as a result of this arrangement will be the ability to increase its capacity and reduce capital expenditures because it will have access to higher quality facilities of the LiTel System. In addition, Charter will incur no maintenance on those facilities. Charter will also be able to reduce expenses by taking advantage of volume discounts available to members of the LiTel System from equipment suppliers. Finally, by virtue of being a member of the LiTel System, Charter will be able to obtain the benefits of the systems network planning process, engineering capabilities, marketing expertise, operational financial analysis capabilities and management information systems support.

The application also states that the note is for a lawful object within the corporate purpose of Charter, is necessary, appropriate, and consistent with the proper performance by Charter of its present and prospective service to the public, will not

³ Case No. 10090, The Application of LiTel Telecommunications Corporation For A Certificate of Public Convenience and Necessity To Provide Intrastate Long Distance Telephone Service To The Public In The Commonwealth of Kentucky And For The Establishment Of Rates.

impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose. Further, Charter states that as a non-dominant carrier, it is only subject to the limited regulation as set forth in Administrative Case No. 273.⁴ All exhibits required of non-dominant carriers have been filed in this case.

Charter is correct in its assessment that it is a non-dominant carrier and therefore is subject to relaxed regulation. However, in addition to the Administrative Case No. 273 Orders, Charter is subject to the requirements of KRS Chapter 278, including KRS 278.300 relating to the issuance or assumption of securities by utilities.

On May 17, 1990, the Commission issued a data request to Charter. Charter responded to the data request on May 29, 1990. The interrogatories posed to Charter were intended to determine if the financing being contemplated by Charter is in compliance with KRS 278.300. The financing arrangement being contemplated by Charter does not appear to be consistent with the requirements set forth in KRS 278.300(3) concerning the necessity and reasonableness of the financing as well as the potential impairment of Charter's operations. This position is based upon Charter's answer to interrogatory number 3, in which it states that no cash proceeds will be received by Charter. It appears that Charter,

⁴ Administrative Case No. 273, An Inquiry Into Inter- and IntraLATA Intrastate Competition In Toll and Related Service Markets In Kentucky.

which was purchased by LCI in Case No. 89-292,⁵ is now paying for the privilege of being acquired by LCI. All of the benefits accruing to Charter through the establishment of this obligation to its parent are exactly those a company would expect to obtain as the result of being purchased by another company with superior resources. In fact, from the answer provided in response to interrogatory number 7, the bulk of the benefits derived from this transaction are classified as "goodwill" on Charter's balance sheet and as noted by Charter are for the purpose of purchasing the "intrinsic" values associated with Charter's affiliation with the LCI network. This is a value that one would expect to accrue automatically as a result of the previously mentioned acquisition.

Charter's non-dominant status does not relieve it of its responsibility to conduct its business, including financings, in compliance with Kentucky statutes. This financing does not appear necessary for the proper performance of Charter's service to the public.

Given the fact that the owners of LCI are the ultimate owners of Charter, the Commission does not understand why this arrangement is being contemplated. Therefore, after reviewing Charter's initial application and responses to the interrogatories, the Commission is not convinced that by entering this

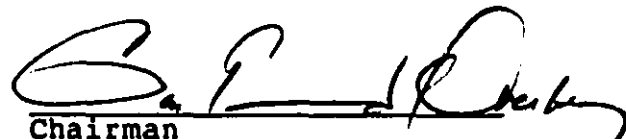
⁵ Case No. 89-292, The Joint Filing of LCI Communications, Inc. And Phoenix Network Corporation For Authorization For The Acquisition Of Phoenix Network Corporation By LCI Communications, Inc. And Subsequent Consolidation Of Phoenix Network Corporation, Charter Management Incorporated, And Charter Network Company LP.

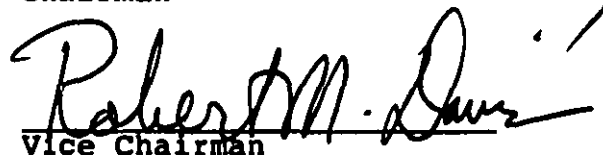
financing agreement, Charter is receiving any benefits which should not have accrued to it as a result of its recent acquisition by LCI. Also the Commission is not persuaded that the interest expense incurred as a result of this financing will not impair Charter's ability to perform its service to the public, especially because on a pro forma basis, the net income of Charter will be a negative amount. As a result and in the absence of any evidence to the contrary, the Commission is not persuaded that the proposed financing conforms to the requirements of KRS 278.300(3).

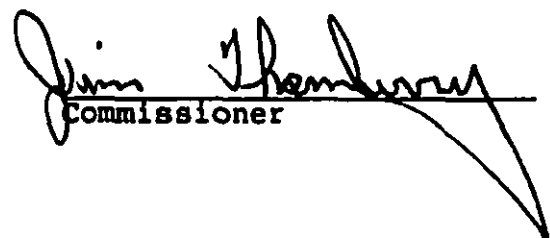
Having considered the record of evidence and being otherwise sufficiently advised, the Commission HEREBY ORDERS that the application of Charter to execute a promissory note to LCI in the amount of \$18,750,000 is denied.

Done at Frankfort, Kentucky, this 11th day of June, 1990.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director